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DEPARTMENT OF STATE

Washington, D.C. 20520

6/5/72 Return to FSE

MEMORANDUM

June 5, 1972

To: E - Mr. Willis C. Armstrong

From: E/ORF - Julius L. Katz KW

Subject: Iraqi Nationalization of IPC

PET 15-2 Iraq

Summary. The parent companies of IPC are unlikely to receive satisfactory compensation for their nationalized properties, and will need our support to keep the Iraqi nationalization from turning the OPEC participation negotiations into a rout. This will mean giving our support to boycott measures, as well as discouraging the French (or Italians, Japanese, or others) from rushing in to fill IPC's position. The Iraqis will be under some financial pressure to settle, and the extent of support they will be able to count on from their OPEC and OAPEC colleagues is uncertain. As the OPEC participation measures move forward, however, a strong line on IPC will be untenable and ways should be examined to salvage some position in Iraq.

US Interests. The value of the American-owned share of IPC's nationalized properties, for which they are unlikely to get satisfactory compensation, is probably no more than $50 million. The oil production which Mobil and Jersey have lost has recently been marginal because of its relatively high cost (a result of the posted price settlements of last winter). It can be argued that the companies brought about their current difficulties by their stubbornness over the 1960 nationalization, and by their manipulation of the production rates of the now nationalized fields; that they had probably in any event written off anything but a most tenuous future in Iraq; and that we should as a result offer them only minimum and pro forma support so as to avoid further antagonizing the Iraqis or other oil producers. While we agree that this argument has some merit, and that we should avoid taking positions which identify the USG totally with the nationalized companies, we believe that our interests in hindering expropriations, and in avoiding a rout of the companies in their dealings with OPEC, dictate that we follow a policy of consistent support for the IPC owner companies and parent governments in demanding and pressing for prompt and adequate compensation.

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Who Will Help the Iraqis? We can assume that the Iraqis will have difficulty selling the nationalized oil, and that the owner companies will use their market power to block sales to the west, at least initially. The Iraqis will be hurt financially even if the southern fields continue to operate and expand production--the potential losses could be in the order of $40 million each month that sales cannot be made. The Iraqis have received oral support from a variety of Arab leaders, including a promise of full support from Libya and a Kuwaiti suggestion that OAPEC establish an emergency fund to help countries under pressure; OPEC has also announced formation of a similar fund. How much support will be in the form of cash, however, remains to be seen--Kuwait will almost certainly contribute, although warily, to its northern neighbor, and Libya will do likewise in spite of its dislike of Iraq's regime. Neither is likely to be overly generous, however, and the Iraqi purse will be even shorter of cash than usual. Syria and Lebanon, which will lose transit revenues, will also feel the pinch until oil produced from the nationalized fields can be marketed in quantity. In short, there will be considerable financial pressure on the Iraqis to reach a new regularization of the situation.

The IPC owners, through their continued operations in south Iraq, will be able to affect the level of their remaining payments to the GOI through decisions on production levels. This lever could be used constructively, to attempt to build some good faith for the compensation negotiations, or negatively to punish the GOI. If the companies attempt the latter, we believe it would be counterproductive. Fortunately, their supply and economic interests probably dictate increased production from the southern fields.

We have no reason to believe that the Soviets encouraged the Iraqi nationalization or that they have promised any financial aid. The Iraqis are capable of running the fields and pipelines with reasonable efficiency and will need only limited technical aid. They will undoubtedly ask the Soviets for aid in marketing the oil. We doubt however if the Soviets will be willing or even able to market large quantities of the nationalized oil.

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Even though they have now agreed to market some nationalized Libyan oil (from the BP concession), the small quantities involved, and the reportedly hard bargain they drove with the Libyans, make it appear likely that they are either unable or unwilling to underwrite the financial success of nationalization measures by the oil producing states. They have considerably more important economic and commercial relations with the OECD countries to consider.

<u>The OPEC and OAPEC Situation.</u> Saudi oil Minister Yamani has used the Iraqis as a bogeyman against the companies in past, and will be able to do so with more conviction in future. More importantly, the Iraqi nationalization will stiffen his position in the participation negotiations; he cannot afford to be completely outflanked by the radicals. The companies appear to suspect that the Iraqi move was cleared, or at least acquiesced in by other OPEC members, particularly the Saudis. (We have no evidence that this was the case; in fact there is some evidence that the Saudis were not informed by the Iraqi intent to nationalize). The companies will want to show as strongly as possible that nationalization is not a workable alternative to negotiated changes in producer relationships. They will ask for our support for boycott and other efforts to prove this point. We will have to support them on this, or risk having the participation negotiations degenerate into a charade. We should keep in mind at the same time, however, that too close an identification with the companies could prejudice our future capability to influence the OPEC governments toward moderation, should the occasion warrant.

OPEC has called a special session June 9 to consider the Iraqi action, at which the Iraqis will request support. Although OPEC officers have said previously that the organization does not advocate nationalization as a policy, the meeting will almost certainly approve the Iraqi move and may make some financial assistance available. Whether the members will also support Iraq by restricting their own oil liftings is considerably more questionable--some members, such as Saudi Arabia, Iran, Abu Dhabi, and Nigeria are now counting on substantial production increases to boost income and would be most reluctant to freeze or restrict their growth. The Iranians moreover have no political interest in supporting the Iraqis.

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The Arab oil producers, who meet in an OAPEC conference June 7 just before the OPEC one, will probably have to go farther--at least verbally--in their support of the Iraqi move. (The just concluded Arab Oil Congress passed a motion of support). The moderates, particularly, the Saudis will be caught between their desire to support the Iraqis against the companies, their annoyance at having their role in the participation negotiations upstaged, and their unwillingness to support the Iraqis at the expense of their own expansion plans. They will probably have to go along, however, with the wishes of the more radical members of the group.

<u>The French Connection.</u> Although the French were offered a special opportunity to come back by President Bakr in his speech announcing the nationalization, the French company (CFP) was treated no differently from the others in the decree. Both the company and French government have announced that they are "carefully examining" the Iraqi proposal, and would undoubtedly like to profit from their closer past relationships with the Iraqis. If we assume that the oil consortium has no chance of regaining its position, then a French-led group would at least be preferable to total Iraqi-Soviet development of this important oil concession. Although this approach may be best for western interests in the long run, any rush into it in the short run would seriously compromise the companies' position in the participation negotiations. We should therefore seek to restrain the French (or others) from precipitate acceptance of the Iraqi overture, and will attempt to bring multilateral pressure to bear toward this end in the OECD Oil Committee meetings next week. The British have in the meantime called... to participation is more clearly established, the companies will need our support in resisting Iraqi efforts to make the nationalization a success. As the participation negotiations move toward defining new company-government relationships, however, a hard line on IPC will become irrelevant and perhaps counterproductive.

Several possibilities might then be explored to maintain some western position in the area:

-- The IPC companies might (though the possibility is slim) be able to capitalize on their continued position in southern Iraq to reenter the northern area as a joint partner with the Iraqis, in return for surrendering a joint partnership in the south.

-- The Iraqi invitation to the French could be converted into formation of a new consortium (The Iranian settlement pattern of 1954). This could involve participation by the French, Germans, Belgians, Italians some US independents, and others (as well as the Iraqis), and would mean that the present owners could realize some compensation from the buyers-in.

There are probably other possibilities as well, but for the moment they are all premature.

E:ORF:FSE:GSBrown:led
6/5/72 ext 20753

Concurrence: E/IFD - Mr. Kennedy

cc: NEA - Mr. Davies
NEA/ARN - Mr. Seelye
NEA/ARP - Mr. Dickman
EUR/SOV - Mr. Kadilis
EUR/FBX - Mr. Biegel
White House/NSC - Mr. Saunders